

Internal Revenue Service

memorandum

WHEARD CC:TL:TS

TL-N-501-90

date: NOV 20 1989

to: Assistant District Counsel, San Diego  
Attn: Alice Harbutte

W:SD

from: Assistant Chief Counsel (Tax Litigation)

CC:TL

subject: [REDACTED] Statute of Limitations

This memorandum is in response to your inquiry sent by Fax on October 16, 1989. This confirms the oral advice which this office gave you on that date.

ISSUE

Whether a consent to extend the statute of limitations with respect to the taxable year [REDACTED] of [REDACTED], a TEFRA S corporation, operates to extend the statute of limitations for assessing the shareholders with respect to the subchapter S items being adjusted.

CONCLUSION

Since, on its face, the consent only purported to extend the statute of limitations for the corporation itself and not for the shareholders, the statute of limitations for the shareholders was not extended.

FACTS

[REDACTED] is an S Corporation subject to the unified audit and litigation procedures of I.R.C. §§ 6241-6245 (TEFRA) for the taxable year [REDACTED]. [REDACTED] has two shareholders, [REDACTED] who jointly own [REDACTED]% of the stock and [REDACTED] who jointly own the remaining [REDACTED]% of stock. The corporation is currently under audit for its taxable years [REDACTED], [REDACTED] and [REDACTED]. The only issue under audit is the amortization of an intangible asset which was listed on the 1120s as "[REDACTED]". The intangible asset was valued at \$[REDACTED] dollars and is being amortized over [REDACTED] years. The statute for the [REDACTED] year was due to expire so the agent obtained an extension from the corporation on the attached

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Form 872 (rather than an 872-S). An 872-S specifically applies to shareholders in TEFRA S corporations. The extension was signed by the power of attorney of the corporation who also had a power of attorney from the individual shareholders. Copies of the powers of attorney are attached hereto as Exhibits B, C, D and E.

#### DISCUSSION

Section 6229, which is made applicable to subchapter S corporations by sections 6241 and 6244, provides:

(a) General Rule.--Except as otherwise provided in this section, the period for assessing any tax imposed by subtitle A with respect to any person which is attributable to any partnership [subchapter S] item (or affected item) for a partnership [S corporation] taxable year shall not expire before the date which is 3 years after the later of-

(1) the date on which the partnership [S corporation] return for such taxable year was filed, or

(2) the last day for filing such return for such year (determined without regard to extensions).

(b) Extension by Agreement.--

(1) In general.--The period described in subsection (a) (including an extension period under this subsection) may be extended -

(A) with respect to any partner [shareholder], by an agreement entered into by the Secretary and such partner [shareholder], and

(B) with respect to all partners [shareholders], by an agreement entered into by the Secretary and the tax matters partner (or any other person authorized by the partnership in writing to enter into such agreement),

before the expiration of such period.

(2) Coordination with section 6501(c)(4).--Any agreement under section 6501(c)(4) shall apply with respect to the period described in subsection (a) only if the agreement expressly provides that such agreement applies to tax attributable to partnership [subchapter S] items.

Thus, the tax matters person, a person authorized by the corporation in writing, or the individual shareholders (but only with respect to themselves) may extend the period for assessing subchapter S items with respect to shareholders. Under section 6229(b)(2), if the extension is contained in an extension of the section 6501 statute, the extension agreement must expressly provide that the agreement applies to tax attributable to subchapter S items. Based, in part, on this provision this office has taken the position that section 6229(a) is a separate statute of limitations from section 6501. Thus, if the period for assessment expires for assessing subchapter S items under section 6229(a), the Service cannot rely on a longer statute of limitations under section 6501 for the shareholders.

It is this office's position that section 6229(a) is the only statute of limitations which will apply to subchapter S items, and is, thus, the only statute of limitations which needs to be extended, unless a case is appealable to the Ninth Circuit. In the Ninth Circuit, the Court of Appeals recently held that, in a pre-TEFRA year at least, not only must the statute of limitations be open for shareholders, it must also be open for assessing tax on the corporation (even though the corporation is not the taxpayer we propose to assess any tax against). Kelley v. Commissioner, 877 F.2d 756 (9th Cir. 1989). The Court in Kelley relied on the language of section 6501 which provides that "the amount of any tax imposed by this title shall be assessed within 3 years after the return was filed." Since both the corporation and shareholders file "returns" with respect to items of a subchapter S corporation, the Court held that both the shareholder and corporation periods for assessment must be open in order to assess tax attributable to flow through items from an S corporation.

Although the period for assessment under section 6229(a) was not at issue before the Court in Kelley, there is a significant hazard that the Ninth Circuit may extend the holding in Kelley to TEFRA years. On the other hand, the Ninth Circuit may find that section 6229(a), which provides that the period for assessing tax attributable to subchapter S items "shall not expire before" certain dates, overrides the limiting language they attributed to

section 6501. Until the Ninth Circuit decides this issue, in cases where the S corporation's principal place of business is within the Ninth Circuit, extensions should be secured for the corporation as an entity as well as for the shareholders under section 6229(b). Pursuant to section 6229(b)(2), extensions with respect to the corporation as an entity under Kelley should specifically extend the statute of limitations with respect to subchapter S items. We may defend statute extensions if only the period under section 6229(a) is open with respect to shareholders. Such cases should be coordinated with this office.

In the instant case, the period for assessment was extended with respect to the "taxpayer" [REDACTED] on a Form 872 expressly limited to certain subchapter S items. Thus, pursuant to section 6229(b)(2) the Form expressly applied to subchapter S items in an extension executed pursuant to section 6501(c)(4). Thus, the form extended the period for assessment for the corporation with respect to the specified items in compliance with the potential requirements of Kelley. However, the form did not purport to extend the period for assessing tax against the shareholders. Thus, the period for assessing tax against the shareholders was not extended.

In conclusion, the statute of limitations was not extended with respect to the shareholders since the consent, on its face, did not purport to extend the statute of limitations for them.

Please refer any questions on this matter to Bill Heard at FTS 566-3289.

MARLENE GROSS

By: Kathleen E. Whatley  
KATHLEEN E. WHATLEY  
Chief, Tax Shelter Branch